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"GOVERNMENTAL AUDITING IN A PERIOD OF RISING SOCIAL CONCERNS"

Down East in Maine, old timers tell a story about the early days of the automobile that seems applicable to what I want to talk about today. This incident occurred when people still used to go "out riding" in their open touring cars--Hudsons, Chalmers, Stutzes, Pierce Arrors, air-cooled Franklins (with the slanting hoods) Dusenbergs, and Model T Fords. It seems that a man from Bangor was driving along one of the back roads, which he knew well, and came to a four corners, or as we say now, an intersection. He noticed that a sign on a post on one of the corners said "Bangor, 5 miles." The peculiar thing about it, as the driver well knew, was that the sign was pointing in exactly the opposite direction. The driver saw a farmer in a nearby field and hailed him: "Don't you know that sign is pointing in the wrong direction? Someone will get lost." "Yea, I know," the farmer replied. "We couldn't put the sign post on the corner where it should have been because there is a ledge there, so we put it on the other side. But it don't make no difference: everybody knows the way to Bangor."

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And I suppose in those far off days, oversimplified in memory, it really didn't make "no difference," as the farmer put it. Compared to the present, most people did know where the roads led because there weren't so many roads, there weren't so many people, and there wasn't that much of a hurry. Well, it does today. The roads to Bangor, to Boston, to Baltimore, or to any place in the United States are well marked now. But many other aspects of the society in which we are traveling are not marked well. Indeed, in some areas of life, if we have even a glimpse of where we are headed we are either fortunate or unfortunate, depending on whether you are an optimist or a pessimist.

What, you may be asking, has all this to do with controllers, accountants, auditors, and financial management? I am here today to try and tell you.

And that phrase, before we get started, reminds me of one more story--quite a different type.

In Washington there used to be a legendary speech writer who rose with his principal through the ranks, from the city council to the state legislature to the House of Representatives to the United States Senate.

There came a time when the speech writer got fed up with his boss. Such had been the relationship between the two that for many years the senator had rarely bothered

to examine drafts of his speeches before the time came to present them.

On this occasion, the solon mounted confidently to the podium and launched into his prepared text. The first page read something like this:

"There are those who say we cannot control inflation and still have full employment. I say we can--and I am going to tell you how.

"There are those who say we cannot contain Communist expansion and still have peace. I say we can--and I'm going to tell you how.

"There are those who say we cannot control riots in the streets and student demonstrations without political repression. I say we can--and I'm going to tell you how."

Whereupon the senator turned the page and found in, the familiar handwriting of his loyal ghost, the following: "O.K., you so and so, you're on your own, I have resigned."

Like the senator, I am afraid that too many of us have long been too complacent that the problems in this period of rising social concerns could be solved by some ghost writer or would solve themselves. They have not been, and won't. And now most of us here, whether in Government or business and industry, know that we have got to find out for ourselves how to solve the problems that beseege us all.

I have labeled the title of this paper "Governmental Auditing in a Period of Rising Social Concerns." In spite

of the highest standard of living in the world, it is perfectly obvious to all that there is widespread social unrest in the Nation, there are demands for changes in National priorities, and there are attacks on our basic institutions which until recently we regarded as "sacrosanct." It is, as the renowned French political historian, Alexis DeTocqueville, wrote more than a hundred years ago:

"The evil which was suffered patiently as inevitable seems unendurable as soon as the idea of escaping from it crosses men's minds. All the abuses then removed call attention to those that remain, and they now appear more galling. The evil, it is true, has become less common but sensitivity to it has become more acute."

And so it is today as all of us in Government and in business attempt to deal with these social concerns through mounting expenditures and a never ending series of new programs.

The accounting profession has a more important contribution to make in these areas--whether private or Government--than you may realize.

Let me begin with a few basic facts and figures. Earlier this year President Nixon submitted to the Congress his budget proposals for 1973, the next fiscal year. His budget calls for expenditures of 246 billion dollars, an increase of almost 10 billion over the estimate for the current year and more than twice the Federal expenditure in 1962.

Even after allowing for inflation, such an increase is startling indeed. It should be to every citizen of our country. Pertinent to our discussion today is what lies behind this increase; growth in the scale and range of

Federal programs which affect virtually every aspect of American life. And the end is not in sight. We face-- as all of you are well aware--tremendous problems in meeting human needs: employment for the employable, better educational opportunities, better health care, better housing and transportation, food for the needy, help for the aged and unemployable freedom from crime--shall I go on?

Our present attempts to deal with these problems center around four major Federal social programs in the Federal Budget--income security, health, education and manpower, and community development and housing. Annual Federal expenditures in the areas increased from 21 billion to 82 billion dollars over the 12-year period 1960-1971. The rate of this increase was much higher than that for National defense expenditures or total Federal expenditures over the same period.

In fact, the 82 billion dollar figure for 1971 that I just cited exceeded expenditures for National defense, by almost 5 billion.

THE GENERAL ACCOUNTING OFFICE:
SCOPE OF AUDIT WORK

These figures of course mean many things to many people-- to some rising taxes, to others another reason to get out of Vietnam. To us at the U.S. General Accounting Office they mean substantially increased auditing responsibility. I assume that most of you know, in a general way, where the GAO, which I head as Comptroller General of the

United States, fits into the scheme of things in Washington. The GAO and my Office was established 51 years ago to assist the Congress in carrying out its responsibility of legislative oversight as to expenditure of public funds.

Being a nonpolitical agency in the legislative branch-- independent of the executive departments and agencies which it audits--GAO has a unique place in the organization of the Federal Government. Appointment of the Comptroller General and the Deputy Comptroller General for 15-year non-renewable terms was designed to insure this independent stature.

The scope of GAO's authority and responsibility has always been broad. The Budget and Accounting Act of 1921 which created the GAO directed the Comptroller General to examine all matters relating to the receipt, disbursement, and or use of public funds, and to make recommendations to the Congress for greater economy in public expenditures. For some time our audit has been moving more and more toward reviews of programs accountability, that is, evaluating the effectiveness of Federal programs and activities. The need for this type of review was specifically emphasized when GAO was directed, in the Legislative Reorganization Act of 1970, to review and analyze the results--the costs versus the benefits--of Federal programs.

Thus, it is evident that, insofar as the Congress is concerned, the scope of the work of its independent auditor with respect to the examination of Federal programs and

activities knows almost no bounds.

NATURE OF AUDIT WORK

In order to serve the need of the Congress for useful and reliable information on how Government programs are operating, GAO must concern itself with three types of accountability:

- fiscal accountability, or fiscal integrity, adequacy of disclosure, and compliance with applicable laws and regulations.
- managerial accountability, or the efficient and economical use of personnel and other resources; and
- program accountability, or whether programs are achieving their intended objectives with due regard to costs and results.

In reviewing the effectiveness of programs having to do with such matters as the environment, education, welfare, health, and housing, GAO is trodding on grounds that are largely unsurveyed. Few standards for measuring performance exist. Planners and managers of programs attacking social ills do not have an over-abundance of information as to how to achieve the most effective results.

Further, there are difficult problems of measuring progress or accomplishment--of knowing where we are--in many of these programs. Our concepts and our methods of accounting for the results of social programs are primitive

at best. Our road signs in these areas are not accurate. As a Nation, we need to develop methods of accounting for these programs that will not only clearly show what we invest in them but what is accomplished in relation to what is intended.

We need techniques to measure the differences in social conditions that result from infusing public funds and other resources into improving those conditions. This type of accounting is needed by policymakers and planners, by managers and operators, and by reviewers of performance, including auditors.

It is a problem to be worked on not only by accountants but by many other professions. It is not an easy problem but it does seem to me to be essential that more rapid progress be made on it than is apparent to date. A system that feeds back understandable information to managers, legislators, and the public on what is being accomplished from spending public funds, should help us do a better job of improving our programs for solving pressing social problems.

One of the steps that we have taken in the General Accounting Office to increase our capabilities for making program evaluations in areas of rising social concerns has been to add to our staff of auditors and accountants specialists in other professions. More than 20 percent of this staff of 3,000 are economists, systems analysts, statisticians, actuaries, engineers, and specialists in administration.

Another step has been to use the knowhow of outside consultants to assist us in developing ways to measure the effectiveness of social programs as well as to obtain expertise in complex technical areas. Still another has been to develop training programs in systems analysis, computer techniques, and statistical methods.

Before getting deeply into any program evaluation, we find out what evaluations the Federal agency responsible has made or has called upon outside organizations to make. We study these evaluations and any published information in the field for use of the results in our own evaluations. We are developing an inventory of mathematical models used by Government agencies and have taken steps toward developing an inventory of program evaluations made, or caused to be made, by all major Federal departments and agencies.

GAO EXAMINATIONS OF INTEREST TO FINANCIAL EXECUTIVES

So much for the nature of our audit work. Now to specific examples, the proof of the worth of what we do. These include the Government's efforts to control water pollution, the Medicare program, and consumer protection activities. Our evaluations of Government programs, of course, have covered many other activities.

WATER POLLUTION

Pollution of the environment--air, water, solid waste--is a matter of great concern to all of us. It is a matter of concern to you as financial executives who must be informed

as to applicable laws and regulations for abating pollution. Also, you must contribute to the resolution of such questions as the choice of methods and equipment, the nature and source of financing, the effect on costs, the location of new plants, and even the economic feasibility of continuing to operate old or marginal plants.

Estimates made last year by the Chase Manhattan Bank suggested that about 10 billion dollars annually is being spent on pollution control efforts nationwide, with the total expected to rise to about 24 billion a year by 1973. But these estimates, large as they are, may already be out of date.

In the past 17 years, the Federal Government has made grants of nearly 3.5 billion to cities and other Government entities to help finance the 12.5 billion construction cost of about 12,000 waste treatment plants. Our review of the construction grant program showed that no systematic approach was being followed in deciding where the application of public funds would do the most good. Frequently, treatment plants were located at points where their effectiveness at removing pollutants was far less than it would have been at some other location.

A more effective approach requires a coordinated and systematic effort on the part of all polluters. During the audit we engaged an engineering firm to assist in demonstrating the usefulness of systems analysis techniques in developing and implementing plans to construct water treatment facilities

for entire river basins and we recommended that such techniques be used in planning for and carrying out water pollution control programs.

MEDICARE PROGRAM

Outlays for Medicare are expected to reach 10 billion dollars in 1973. Our reports to the Congress on Medicare program activities have covered a variety of matters.

In reviews at six hospitals of payments to supervisory and teaching physicians, we found that the hospitals' records showed that the services paid for had, in many instances, been provided by residents and interns whose salaries were also reimbursable under Medicare as hospital services. Where Medicare reimbursed both the physicians and the hospitals, they were paid for such services twice. Proposed legislation would alleviate these conditions.

In another review we found delays in every step of the process of making final Medicare settlements with hospitals and other institutions for services rendered. Some delays were attributed in part to the use of a questionable reimbursement method authorized by the Department of Health, Education, and Welfare. In line with our recommendation, the Department proposed action which it estimated would reduce Medicare costs by about 100 million dollars a year.

CONSUMER PROTECTION, FOOD PRODUCTS

We have submitted five reports to the Congress in recent years on the Federal Government's efforts to protect consumer food products. The titles of these reports tell

their own story.

- Weak enforcement of Federal sanitation standards at meat plants by the Consumer and Marketing Service.
- Better inspection and improved methods of administration needed for foreign meat imports.
- Enforcement of sanitary, facility, and moisture requirements at Federally inspected poultry plants.
- Consumer and Marketing Service's enforcement of Federal sanitation standards at poultry plants continues to be weak.
- Insanitary conditions in the food manufacturing industry.

Food industry establishments subject to Food and Drug Administration inspection include about 32,000 manufacturing and processing plants in this country producing bakery products, candy, carbonated beverages, cheeses, ice cream, chips, jams and jellies, macaroni, and so on.

We requested the Food and Drug Administration to inspect 97 plants selected at random from about 4,500 plants in 21 States, with our auditors accompanying its inspectors.

From the results of these inspections, and using sampling techniques, we estimated that about 40 percent of the 4,500 plants were operating under unsanitary conditions. These conditions, in the opinion of Food and Drug Administration officials, would be representative of conditions at plants nationwide.

Our coverage was designed to show the dimensions of unsanitary conditions in the food manufacturing industry; and to suggest to the Congress ways that the Food and Drug

Administration's inspection methods could be improved so that the American people can have more confidence that the food products they buy are processed under sanitary conditions and are safe, pure, and wholesome to eat.

CONSUMER PROTECTION, BIOLOGICAL PRODUCTS

In a report on problems relating to the effectiveness of influenza vaccines, we pointed out that the National Institutes of Health had not required biological products to be effective as a condition of licensing prior to 1962, when a requirement for efficacy was added to the applicable law. Although we found no evidence of any ineffective biological products being licensed after 1962, we did find that ineffective products licensed prior to 1962 continue to be marketed.

Also, during 1966, 1967, and 1968, NIH permitted the release of 221 lots of influenza virus vaccines of which, according to the manufacturers' tests, 115 failed to meet established potency tests. NIH was releasing vaccines even when its own tests showed the potency to be as low as 1 percent of the established standards.

Senator Ribicoff stated that this report, along with others established the need for comprehensive legislation to protect American consumers, including the creation of an independent Consumer Protection Agency.

FEDERAL AID TO STATE AND LOCAL GOVERNMENTS

Federal grants for programs intended to cope with problems of social concern made to State and local Governments increased from 71 programs and 2 billion dollars in 1950 to 530 programs

and 24 billion in 1970. They totaled 30 billion in 1971.

Expenditures called for in the President's 1973 budget proposal, total 43.5 billion, an increase of 4.4 billion over the estimate for 1972. Such Federal aid constitutes over 20 percent of the revenues of the State and local Governments.

It is GAO's responsibility to examine into the manner in which the Federal grantor agencies discharge their responsibilities under these programs. Grantor agencies and the State and local Governments also have a responsibility for examining into the manner in which their agencies carry out these programs and account for the use made of grant funds.

Although most Federal departments and agencies have professional audit staffs, there is considerable room for improvement in the scope and quality of auditing of grant programs. Auditing at State and local levels is in various stages of development. Many auditors for the State and local Governments extend their reviews of fiscal accountability to encompass matters of economy and efficiency of operations. However, very few have made much progress in examining into whether funds are being spent only in furtherance of program objectives, whether programs are achieving the intended results, and whether better results could be achieved through alternative methods, with due regard for costs.

The magnitude of the audit work required under grant-in-aid programs makes it impossible for Federal grantor agencies responsible for administering the programs to make

detailed examinations of all programs. The extent to which reliance can be placed on audits made by or for State and local Governments will depend on the auditing capability available either through their own organizations or through the independent public accountants, and on the breadth, depth, and quality of the audits conducted at these levels.

We do not believe that current audits in State and local Governments, with some exceptions, provide sufficient information to permit a judgment on whether grants funds have been spent with due regard to economy, efficiency, and effectiveness and in compliance with laws and regulations governing the use of those funds.

Naturally, our office has been concerned about this problem. We are engaged in a major effort, with the cooperation of eight of the Federal agencies having large grant programs, to develop a body of standards for guidance in auditing Federal grant programs. We hope to publish these standards by the end of June. However, they are only a beginning of the effort needed to improve audit capabilities. These audit standards will define more clearly the nature and quality of auditing needed to provide legislators, other policy-makers, and managers with information and independent evaluations on what is done and what is accomplished with grant funds.

Having audit standards is one thing. Applying them is another. We expect these standards to be applied by all agencies of the Federal Government in their audits of federally

assisted programs. We expect these agencies to encourage the adoption of these standards by State and local auditors and by independent public accountants making audits for State and local Governments.

REVENUE SHARING AND ACCOUNTABILITY

The need for adequate accountability systems and effective auditing in State and local Governments will become even more important if the concept of revenue sharing is adopted.

The amount of 43.5 billion for Federal aid to State and local Governments, proposed by the President for 1973, includes 5 billion for general revenue sharing with State and local Governments and additional amounts for special revenue sharing. It appears, however, that a bill introduced by Congressman Wilbur Mills, Chairman of the House Ways and Means Committee, is likely to be enacted with some modifications, by the House. That committee has approved a bill calling basically for payments of 5.3 billion annually over a 5-year period--1.8 billion to the States with no restrictions and 3.5 billion to local Governments to be used for public safety, public transportation, or environmental protection.

Revenue sharing has been a controversial proposal, particularly the concept of turning Federal revenues over to State and local authorities with no restrictions on how they may be used and little, if any, accountability to the Federal Government as to how they are spent. If some degree of accountability is not built into the legislation, the

fundamental tenet of American democracy that holds the taxing authority accountable for the effectiveness with which the tax revenues are spent would be violated. The audit standards that I referred to earlier may well become a major accountability tool for the Federal Government under the revenue sharing procedure.

DEPARTMENT OF DEFENSE EXPENDITURES

Many of the companies you represent are engaged in furnishing supplies and services to the military departments whose expenditures have become a matter of rising social concern. The basic cause for this concern has been the increased demand for allocating more and more of the Nation's resources to the resolution of the problems of our society. Opposition to the war in Vietnam, publicity on such matters as cost overruns on Government contracts, and the sheer magnitude of military expenditures have added fuel to the concern. Establishment of the Commission on Government Procurement and the Cost Accounting Standards Board--two actions evidencing the concern of the Congress--are matters of direct concern to many financial executives.

The Procurement Commission was established to conduct a broad study of the Government's current procurement statutes, regulations, policies, and procedures, and the problems arising thereunder. The Commission--of which I am a statutory member--is expected to make its recommendations to the Congress toward the end of the year.

I recently established a separate procurement division within the GAO which is concerned primarily with conducting audits and recommending improvements in Government procurement procedures, practices, and organization. This will not only improve our capability to audit this 50 billion a year business but it will enable us to follow through and assist the Congress more effectively in reviewing the Commission's recommendations.

The Cost Accounting Standards Board was established as an agent of the Congress to develop and promulgate cost accounting standards for use by defense contractors and sub-contractors. GAO had previously made an 18-month study at the direction of the Congress and found such standards feasible and desirable.

On February 24, 1972, the 5-member Board, of which I am chairman, sent to the Congress the first of its regulatory issuances and two proposed cost accounting standards. These materials included a regulation requiring defense contractors to disclose their cost accounting practices as a condition of contracting, and to follow those practices consistently.

One of the proposed standards, "Consistency in Allocating Cost Incurred for the Same Purpose," is designed to eliminate a prevalent cost accounting problem--instances in which the same type of cost is charged to a contract both as a direct cost and as a share of indirect costs. The other proposed standard, "Consistency in Estimating, Accumulating and

Reporting Costs," is designed to insure that a contractor's practices used in estimating costs for a contract proposal are consistent with the cost accounting practices used by him in accumulating and reporting costs incurred. Government procurement regulations have not previously contained this kind of requirement,

These first standards and regulations will become effective on July 1, 1972, unless the Congress by concurrent resolution states that it does not favor them. The documents referred to were published for comment in the Federal Register on December 30, 1971. In addition, they were mailed on that day to 175 persons or organizations which had indicated a desire to comment on them or had assisted the Board in its early consideration of the proposed measures. After the responses were considered, the documents finally promulgated were strengthened and improved. The extensive response and cooperation by industry, the accounting profession, and Government agencies has made an important contribution to the Board's efforts.

I would like to insert at this point a special note of thanks to the Financial Executives Institute for its cooperation in this undertaking. As most of you no doubt know, the Institute through its Committee on Government Business, and five subcommittees, is assisting us in research for developing proposed standards and testing them at individual contractor plants. This is precisely the type of interest

and support which the Cost Accounting Standards Board needs in order for the Government to propose standards that are workable and practicable for all concerned in business and industry. This is much appreciated.

In addition to making examinations required by acts of Congress and others requested by congressional committees, the General Accounting Office makes many examinations on its own. One example is the series of reviews we are making of major weapon systems during the various stages of the acquisition cycle.

The primary objectives of these reviews are to determine the basic causes of cost growth, schedule slippage, and deterioration of the originally expected performance characteristics in order to make recommendations for improving the weapon acquisition process. Also, we believe that our reports on these continuing reviews provide a means of keeping the Congress and appropriate congressional committees currently informed on the progress and status of the major programs in the weapon acquisition process and assist them in making decisions on the authorization and appropriation of funds for the programs.

Our 1971 report was used extensively by the Armed Services and Appropriations Committees of both the Senate and the House during hearings on fiscal year 1972 spending authorizations and appropriations for the Defense Department. We expect that similar use will be made of our 1972 report.

CONCLUSION

I have referred to our concerns with the programs of the Department of Defense in the context of a paper on rising social concerns because it is one way in which we can provide the Congress information--and assurance wherever possible--that these programs are being carried out economically and that the Defense Department is managing its resources prudently. This concern is relevant to those who are challenging priorities and who are saying that we could safely cut defense spending and apply those funds more usefully to unmet social needs.

Even more importantly, one of the most serious consequences of the social frustrations and disappointments of many groups in our society is the loss of confidence and credibility in Government itself. The President voiced this concern when he said in his State of the Union message last January:

"Let's face it. Most Americans today are simply fed up with Government at all levels. They will not--and should not--continue to tolerate the gap between promise and performance in Government."

One way we can restore such confidence is to insure that funds entrusted to Government are effectively and efficiently spent. The cost of failure in this respect is not so much the loss of the money itself--in that it could have been spent better elsewhere--but in the ability of the Government to perform as it should perform--to produce results.

In all of this, the auditor plays an increasingly important role, particularly as he moves in the direction

of assessing management, methods, and the effectiveness with which funds are spent. He must concern himself with questions of failures of coordination, with duplication, with jurisdictional delays, the persistence in using outmoded methods--these and many other problems which create a gap between promise and performance.

For the auditor to be effective in this expanding role, he must have available to him expertise in many new areas--engineering, statistics, systems analysis, and so forth--but most importantly, he must have information which provides the data necessary for both operations and for evaluation. Moreover, he must have standards of performance against which he can make useful judgments. These skills, this information, and these standards are not easy to come by--particularly when we are dealing with social programs.

What are the standards against which we can evaluate social programs? The first test is whether we can define clearly our objectives in law or regulation. Can we define the information at the outset that we need to evaluate the program at a later point in time? Have the program agencies assessed priorities? Has there been an effort to reach a consensus as to an acceptable rate of progress? What is an acceptable rate of reduction of accidents, of disease, and drug addiction? How do we devise tests for progress in resolving such apparently irresolvable issues as finding a cure for the common cold or reducing noise pollution?

No one doubts the practical difficulties of assessing the cost and benefits of social programs and of evaluating the impact of these programs in many situations. In the final analysis, the hard choices will be political choices--our whole political system is built around this fundamental fact--but political leaders and the public need increased awareness of the arguments pro and con of the choices that must be made. And it is in this area that the auditor at all levels of Government can plan an increasingly important role.

Factors causing the Nation's rising social concerns have also resulted in increased burdens and responsibility, as well as opportunities of financial executives in business and industry. They, like Government auditors, must gear themselves to demonstrating higher standards of accountability in the public interest and, in fact, they appear to be doing so already.

But, as I have said, and repeat for emphasis, the most immediate need and opportunity for improved and broadened auditing is in the area of State and local Governments, including work performed for them by public accountants. They must raise their sights to the level of determining how effective these programs really are in achieving the purposes intended.

Working in cooperation with Federal auditors, they must direct more training and more work toward determining whether today's programs--supported by dollars which the taxpayers work hard to earn--are delivering results that

are economical, efficient, and, most important of all, effective.

This is the public's interest in all this and it must be upheld now and for as far into the future as the road signs point.

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